Financial Accounting Standards Board

International Accounting Standards Board

To:	FASB, IASB, Joint International Group, and Financial Institution Advisory Group Members
From:	Financial Statement Presentation Team
Subject:	Summary of the December 6, 2010 Financial Statement Presentation Working Group Meeting
Date:	December 6, 2010

The audio and video of the full day's discussion are available at www.fasb.org and www.ifrs.org respectively

Location: Norwalk, CT

Topic: Financial Statement Presentation

Basis for Discussion: Working Group Papers 1 – 7

Length of Discussion: 8:00AM to 2:00PM

Attendance:

Staff in charge of topics:	In Norwalk: Nick Cappiello and Kevin Catalano In London: Stephen Cooper, Holger Obst
Other staff at table:	In Norwalk: Regenia Cafini and Chandy Smith In London: Takashi Matabe
JIG members present:	In Norwalk: Gregory Jonas (Morgan Stanley), Hiroshi Yamada (Panasonic Corporation), Ken Kelly (McCormick) In London: Kathryn Cearns (Herbert Smith), Jacque De Greling (IXIS Securities, by phone), Sue Harding (Standard & Poor's), Stuart MacDonald (Scottish Power plc)
FIAG members present:	In Norwalk: John Gallagher (UBS, for Ralph Odermatt), Stephen Ryan (NYU Stern School of Business), Karen Stothers (Basel Committee on Banking Supervision), Alan Zimmerman (Macquarie Group), Lauren Belot (All State) In London: Rob Esson (NAIC), Jo Clube (Aviva PLC)

FASB members present:	In Norwalk: Tom Linsmeier, Larry Smith
IASB members present:	In London: Stephen Cooper (chair), Patricia McConnell, Jan Engström, Darrel Scott
Official observers present:	Irina Ipatova (EFRAG)

Objective of the Meeting

1. FASB and IASB members and staff met with members (including an official observer) of the Joint International Group (JIG) and Financial Institutions Advisory Group (FIAG) on December 6, 2010, to discuss the Staff Draft for the Financial Statement Presentation (FSP) project. Meeting participants discussed the following topics:

   - Working Group Paper 1, *Outreach activities*
   - Working Group Paper 2, *Cohesiveness principle, sections and categories, and statement of financial position*
   - Working Group Paper 3, *Statement of cash flows*
   - Working Group Paper 4, *Disaggregation of income and expense items*
   - Working Group Paper 5, *Analysis of changes and remeasurements*
   - Working Group Paper 6, *Next steps*
   - Working Group Paper 7, *Financial services entity issues*

Working Group Paper 1: Outreach activities

2. Working group members praised the staff for their outreach efforts and generally felt that the outreach efforts provided a sufficient basis from which to continue developing the FSP Exposure Draft (ED).

3. Working group members questioned the usefulness of the statement of cash flows for financial institutions around the globe. The feedback from users was consistent in that analysts do not use the current statement of cash flows because it does not provide useful information. Analysts of manufacturing companies, on the other hand, find the statement of cash flows useful and were supportive of the proposal for the direct method statement of cash flows. Further conversation on this topic was reserved for the time devoted to the cash flow paper.

4. A question was asked as to how the user outreach was performed. The staff explained that they spoke with analysts of manufacturing entities separately from analysts of financial services entities. Most analyst meetings lasted about two hours. One of the working group members who had participated in the analyst outreach explained that their group held two sessions before meeting to educate meeting participants on the proposals and gave them time to think about the implications.

5. Feedback received by the European Financial Reporting Advisory Group (EFRAG) was also discussed. The most controversial issues they found were: disaggregation, the direct cash flow statement, scope, the definition of financing, and remeasurements. The EFRAG's respondents questioned the need for a new presentation. They also indicated a desire for evolution as opposed to a revolution and stressed the urgent need for fixing fundamental issues related to the performance statement (namely, what items should be presented as components of other comprehensive income and whether to allow recycling) before addressing the issues related to this project.

Working Group Paper 2: Cohesiveness principle, sections and categories, and statement of financial position

6. A board member asked the staff about the support for or confusion about the definition of the financing section. The staff explained that some constituents view anything that bears interest as financing, and that most preparers and users are comfortable with the financing section. They said that some constituents would prefer for the financing section to contain all items that would normally be managed by an organization's treasury function. This would include cash. They also explained that there were some misunderstandings about the operating finance subcategory with respect to which items should be classified therein.

7. Another staff person said that U.S. users were supportive of the classification and categorization criteria in the Staff Draft. She explained that U.S. users would prefer more prescriptive classification criteria in order to increase comparability, and that users in the U.S. were more supportive of the financing section than non-U.S. users. She said that many U.S. users thought that some operating finance items should be classified as financing. Working group members are generally supportive of cohesiveness.

8. One working group member said that while she does not fully support the operating finance subcategory, she understands that subcategory and is amenable to making no changes in an ED. The same working group member said that she still has trouble understanding how a financial service entity can properly apply the classification criteria.

9. A Board member explained that a distinction needs to be drawn between comparability and uniformity in the presentation of financial statements. He asked the working groups why users view uniformity as important while preparers do not. One working group member explained that she believes uniformity is not desirable, but that some measure of flexibility should be used in the classification criteria. She believes that rigid criteria (i.e., uniformity) will reduce comparability in financial statements, and that the criteria in the Staff Draft are too rigorous. The same working group member said that, despite her belief that more flexibility would be preferable, she understands the logic for an operating finance subcategory and is not opposed to that subcategory.

10. One working group member explained that he believes rigidity and flexibility can both be achieved by writing a standard with very rigid principles, but which adds the ability for management to classify things according to the way in which the accounts/items are managed. He explained that cash should be in financing if an entity's treasury function manages cash and debt together. This working group member disagrees with eliminating the notion of cash and cash equivalents. He said that he manages his cash and cash equivalents in exactly the same way and he thinks that the "cash" number on many companies' balance sheets will be reduced to zero under the Staff Draft due to the use of sweep accounts.

11. One working group member asserted that a management approach could be very enlightening for an analyst, because it would allow the analyst to compare the reasons different companies believe they are different from one another.

12. One working group member asked the staff to be cognizant of the large amount of joint ventures in which entities participate. He believes that joint ventures should be classified in the operating category of the Statement of Financial Position (SFP)The staff agreed that the operating category is the best place for most JVs, and confirmed that the staff will be mindful of the words used to describe the operating and investing categories.

13. The staff responded to the working group members who raised concerns about the classification of cash by asking if they would prefer to see two “cash” numbers – one for cash used in operations and one for cash used to manage debt. One working group member said that she tries to separate it today, so being provided with two cash numbers would be an improvement. Another working group member said that she has seen management explain a similar type of division in SEC filings, and so maybe the FASB should attempt to draw a distinction between the two different types of cash balances. A Board member asked if talking about cash was at all helpful for the working groups, since users’ primary need is to have cash clearly separated from other items so as to draw their own distinction. The staff explained that they have heard many differing arguments for the classification of cash, with the only consistency being that constituents do not want to see cash in the investing category. One analyst in the working group explained that as long as the criteria for classifying cash are sufficiently rigorous, analysts will be agreeable. He explained that ensuring consistent application by companies is vital to a properly working standard.

14. One working group member explained how to achieve comparability as follows: Where the facts are the same, the accounting should be the same; but where business models drive differences in the facts, then a management approach is preferred. When it is a question of differing facts, rigor and prescriptiveness need to be used. This working group member explained that useful financial information is three-dimensional. The three dimensions are nature, liquidity, and purpose. He believes that trying to incorporate all three dimensions into the face of financial statements makes them look cluttered. At least one element can be properly moved to the notes.

15. A working group member explained that disaggregation is the most important element of comparability. He asserted that since all users rearrange financial statements according to their own methods and preferences, a management approach is preferred. He believes allowing management to decide on the classification could be enlightening.

16. When asked about the format of the SFP they preferred the alternative shown in the appendix to Paper 2. This presentation more closely resembles today’s Balance Sheet. One working group member expressed some apprehension about the presentation in the

appendix due to cost concerns. Another working group member explained that cohesiveness is not costly, but that disaggregation introduces the significant costs.

17. One working group member asked the staff whether there is support for the classification criteria among financial services entities and their users. The staff answered that most people believe that the categorization is operable for financial services entities, but most everything will likely be classified in the operating category. One working group member asserted that such a constructive elimination of the investing category as useful. The staff asserted that users of manufacturing companies' financial statements were supportive of the separation and definitions of the operating and investing categories.

18. One working group member explained the investing category, could potentially become an "orphan category signaling to investors that the investing items are neither important nor necessary to the company's business. He does not view any amounts in his financial statements as "investing" items.

19. One working group member stated that financial statements need a high level of comparability: one of the key features of financial statements is to provide easily usable information, which can be understood without having an in-depth understanding of the accounting standards which drive them. A management approach should be limited. The same working group member explained that from a European perspective, but also with the prospect of convergence in mind, we should not forget that the primary reason for using a "single high-quality standard" should be to provide comparability.

20. Some working group members reminded the staff that the "first users" of financial statements are often data aggregators, and not analysts.

Working Group Paper 3: Statement of cash flows

21. One working group member indicated that the only people in Europe that support the direct method statement of cash flows (SCF) are academics. Another working group member felt that some users might find a direct method SCF useful if they understood how to use it. This member, however, questioned the benefits of the requirement if people do not know what the numbers mean or how to incorporate them into their analysis.

22. In general, working group members questioned whether the benefits associated with this proposal outweigh the costs. Most working group members felt that similarly beneficial information could be obtained in less burdensome ways and supported several of the alternatives the staff presented. Those alternatives included disclosing supplemental cash flow amounts that users have indicated would be useful in their analysis (e.g., cash from customers or cash paid for interest, etc.), providing information about the changes in balance sheet accounts that would assist a user in discerning cash flow amounts, and/or disaggregating the changes in balance sheet accounts presented in the statement of cash flows to align with the line items presented on the SFP.

23. Despite the favorable cost-beneficial relationship of disclosing supplemental cash flow information, one working group member questioned the practicality of such an approach when not all users are looking for the same information. One working group member suggested that rather than prescribing specific items, perhaps a principle could be developed that requires a company to disclose the key cash inflows that drive revenues as well as the key cash outflows that are used to support the primary operations.

24. Working group members generally felt that the SCF for financial institutions is not useful and that significantly increasing the costs to obtain only marginally useful information would not be cost-beneficial. One working group member noted that nobody uses the direct method SCF currently provided by Australian financial services entities. Furthermore, several working group members suggested that important information can be obtained in other ways. For example, the Board could address the stickiness of deposits through liquidity disclosures rather than through the cash flow statement or simply by subtracting year-to-year balances on the SFP.

25. During their discussion concerning the SCF for insurers, one working group member pointed out that the statement is meaningless because some cash flows relate to policyholders while others relate to participation in the return on investments. However, this working group member felt that improving the cash flow statement for insurance entities was important. She reasoned that requiring companies to disclose surplus returns would help shareholders see how much of the return is available to them. A working group member also indicated that if the Boards decide to allow an indirect-method SCF

with additional disclosure requirements, those additional disclosures might include, among other things, claims paid and premiums received.

26. Another working group member also felt that improving the SCF for insurers was important. He explained that a direct-method SCF would, in fact, be useful to users of insurance entities. He explained that the investing and financing portions of an insurer's SCF (which are presented in a direct format) help users see how the company is being run and understand how management makes decisions. He believed that investors would use information from a direct cash flow statement if they had it; however, users cannot use what they do not have.

27. Though many of the issues brought up in regards to insurance entities can be dealt with in the insurance project, working group members generally agreed that the FSP team should be involved.

28. One other issue working group members discussed was cash and cash equivalents. One working group member suggested clarifying cash and cash equivalents in separate investing cash flows and wondered if there was a way to make the distinction between cash and cash equivalents less restrictive. This member felt that companies should be able to adjust noncash items that are cash-like depending on the way the business uses them.

Working Group Paper 4: Disaggregation of income and expense items

29. One working group member said that, because most analysts use segment information for their analyses, it would make sense for a standard to require disaggregation at the segment level.

30. One working group member stated that convergence should be the goal and that any step toward an unconverged standard would be a step in the wrong direction. Another working group member agreed and said that convergence is more important on this project than on any other project. These working group members stated these opinions in reference to the post-implementation review of IFRS 8 by the IASB. The general feeling among those who made similar comments was that either the IASB should hurry the process along or the FASB should wait before making any changes to the guidance on segment reporting until the review is complete.

31. One working group member said that his company does not and cannot obtain by-nature information at the segment level, and that he doesn’t usually have that information at the business unit level. Individual departments of his organization track by-nature information, but that information is not preserved at a level higher than department. The same working group member explained that he has a reasonable idea of the percentage breakdowns of the by-nature costs for labor, materials, and overhead, but that they are not precise. He agreed that there are some problems with the current segment reporting guidance, and that some additional information may be useful to users, but stated that he personally would not prefer expanded segment disclosures. Another working group member agreed that obtaining by-nature information for individual segments would be difficult and costly.

32. One working group member suggested that by-nature information is so different from company to company that it would be useless in the hands of an analyst.

33. A working group member stated that by-nature information can definitely be captured and recorded at the source if the entity chooses to. He said that questions such as “why are margins declining?” cannot be answered honestly without by-nature information. He views by-nature information so basic and essential to writing an MD&A and understanding the business that he doesn’t know why a company should not be required to report it. Another working group member stated that companies have analyses about changing margins and can explain them when asked, but companies do not collect the information based on raw materials, labor, etc. These two agreed that the information is used by management; just not in the way a typical analyst or investor would use the information.

34. One working group member said he could probably break functions and/or segments down by nature if he had to. This working group member works for a large utility.

35. One working group member said that some constituents have observed the by-nature requirements in Staff Draft as a move toward requiring reporting fixed and variable costs. He cautioned against ever requiring that information, because preparers are still arguing about whether some costs are fixed or variable.

36. The staff asked the working groups which, if any, of the alternatives from paper 4 they would prefer.

    a. One working group member said that 4, 5, and 6 would be acceptable.

    b. Another said that 1, 2, 3, and 5 would be better.

    These are the only two working group members who responded about the alternatives. There was no consensus about what alternative information would be most cost beneficial.

37. One working group raised the question of outsourcing: Does it make sense for one company to report labor costs as labor costs while another company reports the exact same activity under another label since those costs are outsourced to a third-party provider?

38. One working group member asked if the new disclosure requirements might cause information that is immaterial to be disaggregated. They suggested that disaggregating truly immaterial amounts just for the sake of disaggregation fails a cost-benefit test.

Working Group Paper 5: Analyses of changes and remeasurements

39. Working group members were generally supportive of the analyses of changes and remeasurement disclosures; however, there were some concerns over the cost. One working group member suggested costs could be minimized for the analyses of changes by allowing companies to present indirect numbers (which is not inconsistent with their use of indirect cash flows today); however, indirect numbers are harder to audit. Alternatively, the Boards could prescribe the accounts to be rolled forward and then require companies to present other relevant information that is specific to their operations.

40. A working group member suggested that the relief provided by withdrawing the requirement for a direct method statement of cash flows would be nullified if companies still had to provide cash inflows and outflows as part of the analysis of changes. This working group member suggested requiring companies to disclose important information from significant balance sheet accounts rather than a rollforward.

41. One working group member thought seeing the change in working capital would be useful, but questioned preparers on whether the costs would be significant to obtain such

information. A working group member who was a preparer indicated that his company did an indirect cash flow for working capital items manually. Taking the disclosure requirements to the next level would require significant systems changes. They can, however, back out significant items; the leftover amount would be the change in cash. He suggested only requiring the major components to be disclosed.

42. Concerning remeasurements, one working group member indicated that they would be extremely useful and suggested the staff leave it as originally proposed. Another working group member felt that requiring a description of the nature of the remeasurement would be helpful as "unusual" or "remeasurement" would not advance their analysis. This same member also felt linking those remeasurements to the financial statements would be useful.

43. Working group members asked questions with regard to what investors wanted to see. The staff explained the feedback they received from users, who indicated a desire to see how receivables are netted against discounts as well as additional disclosures around remeasurements that are included in income. They are interested in additional disclosures around level 3 remeasurements, but the staff noted that level 3 already has specific disclosures required.

44. The staff also explained that some users felt that the realization of gains and losses should not be included in the remeasurement, but there was not a consistent view. One working group member responded that a majority of the balance sheet is carried at fair value, therefore, she absolutely wanted to see the realization of gains and losses in the remeasurement note. This working group member suggested the Boards consider which remeasurements are most relevant.

Working Group Paper 6: Next steps

45. A Board member asked the working group members to all comment on the following five areas:

    a. OCI and performance reporting

    b. Primary statements

    c. Segment reporting

d. Cash flow

e. Disclosures.

All the working group members were given a chance to voice their opinions on these topics as they related to FSP.

46. All working group members believe that the Boards should delay issuing an ED until all of the “major projects” are completed. Every member would also prefer a transition period of several (five to seven) years. One working group member believes that the effective date should be at least two years after the implementation of the other “important projects.” Some working group members believe that the Boards should signal the expected delay in issuing an ED to constituents.

47. One working group member stated that all of these issues are important and they would like to see the Boards publicly prioritize them so the public can know. Some members expressed that the priority should not lie with this project at this time.

48. One working group member stated that ten years from now, the Boards’ decision to require a single statement of comprehensive income could be the most important development in financial reporting of this decade.

49. One working group member stated that information in the face of financial statements is relied on more heavily than information in the notes. This working group member would like to see future developments on the project focus on ensuring that the correct amount and type of information gets reported in the notes.

50. Several working group members believe that the Boards should define other comprehensive income before moving forward. One working group member reminded the Boards that this project began as a “performance reporting” project and they still have not decided which measure of performance is most important to report.

Working Group Paper 7: Financial services entity issues

51. A Board member asked the working groups to give their impressions on whether financial institutions should have different presentation, disclosure, etc. than industrial/manufacturing companies.

52. All members agreed that financial institutions are different from most other entities and that the differences should at least be addressed by the Boards for the ED. Some working group members were supportive of allowing/requiring completely different financial statements and disclosures from financial institutions, while some were more cautious, reminding that financial institutions are competing for the same investors' capital.

53. One working group member referred to a particular financial institution's use of"items to be hedged to how they're hedged" reconciliation as a potential improvement to financial reporting for financial institutions.